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UNIVERSITY OF MONTANA

REPORT ON EXAMINATION OF FINANCIAL STATEMENTS

Conducted Under Contract by Ernst & Ernst,
Certified Public Accountants

Fiscal Year Ended June 30, 1976

OFFICE OF THE LEGISLATIVE AUDITOR
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UNIVERSITY OF MONTANA

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Fiscal Year Ended June 30, 1976

76C-28

STATE OF MONTANA

Office of the Legislative Auditor

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HELENA, MONTANA 59601
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September 19, 1977

The Legislative Audit Committee
of the Montana State Legislature:

Transmitted herewith is the report on the audit of the University of Montana for the year ended June 30, 1976.

The audit was conducted by Ernst and Ernst, CPA's, under a contract between the firm and our office. The comments and recommendations contained in this report represent the views of the firm and not necessarily the Legislative Auditor.

The agency's written response to the report recommendations is included in the back of the audit report.

Respectfully submitted,

Morris L. Brusett

Morris L. Brusett, C.P.A.
Legislative Auditor

Report of Comments and Recommendations
and Audited Financial Statements

UNIVERSITY OF MONTANA

June 30, 1976

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SUMMARY OF RECOMMENDATIONS

As a separate section in the front of each audit report we include a listing of all recommendations together with a notation as to whether the agency concurs or does not concur with each recommendation. This listing serves as a means of summarizing the recommendations contained in the report and the audited agency's reply thereto and also as a ready reference to the supporting comments. The full replies of the University of Montana and the Commissioner of Higher Education are included in the back of this report.

	Page
Thoroughly review and analyze its present management information system, identifying desired system improvements and enhancements, and expend such efforts as necessary in order to integrate the present costly and segmented accounting system into a comprehensive management information system.	2
Agency Reply: Concur. See page 62.	
Develop comprehensive accounting and budgeting procedure manuals.	3
Agency Reply: Concur. See page 62.	
Prepare monthly financial statements on a timely basis showing (as appropriate) the financial position, revenues, expenditures and other changes, and changes in fund balances for each fund.	3
Agency Reply: No response.	
The chart of accounts be revised in order to be more compatible with the University's organizational structure and the financial reports to be generated.	4
Agency Reply: Concur. See page 63.	
Conduct such an organizational review of data processing activities to determine appropriate staffing levels.	5
Agency Reply: Partially concur. See page 63.	
Establish procedures restricting access to computer operations only to authorized employees, and perform a detailed review of data security for purposes of identifying needed refinements. Furthermore, that a written disaster plan be developed.	5
Agency Reply: Concur. See page 64.	

SUMMARY OF RECOMMENDATIONS (Continued)

	Page
Establish a continuing education program to ensure that the level of data processing knowledge is continually kept current in both the operations and programming sections.	6
Agency Reply: Partially concur. See page 64.	
Develop a long-range systems plan to ensure that new systems under development will easily integrate with other systems.	6
Agency Reply: Concur. See page 65.	
The operations section manager sign or initial the console log to indicate that such review was made.	7
Agency Reply: Partially concur. See page 65.	
Adequately documented input, processing and output schedules be developed for each application.	7
Agency Reply: Concur. See page 66.	
Consideration be given to the development of a cost allocation algorithm whereby user departments can be charged based on actual usage.	7
Agency Reply: Partially concur. See page 66.	
A manual be created establishing standards for programming, system design, management, documentation and methods.	8
Agency Reply: Concur. See page 67.	
Develop adequate procedures to ensure proper system documentation, including general narratives, system flowcharts and standard formats.	8
Agency Reply: Concur. See page 67.	
Develop detailed data entry instructions.	8
Agency Reply: Concur. See page 67.	
That the need for an automated "jobs in progress" system be monitored in light of current and projected levels of data processing activity.	9
Agency Reply: Concur. See page 68.	

Page

The internal audit department develop and implement such programs. 9

Agency Reply: Concur. See page 68.

That source documents be used to support all input changes for purposes of creating an adequate audit trail. 9

Agency Reply: Concur. See page 68.

That user job request forms be prepared (with adding machine tapes attached) to assist in the balancing process. 10

Agency Reply: Concur. See page 69.

The payroll department check the information processed by data processing to verify such information as the number of timecards, number of regular and overtime hours, salary rates, etc. 10

Agency Reply: Concur. See page 69.

The payroll system be modified to accept batch numbers to aid in balancing input data. 10

Agency Reply: Concur. See page 69.

Edit routines in the payroll program include batch total checks. 10

Agency Reply: Concur. See page 69.

Certain key information fields, such as pay rates, be put on the payroll master file at the time of employee hire, and that control procedures be established for any future changes to the file. 10

Agency Reply: Concur. See page 70.

Specific information relating to input field controls be conveyed to each department. 11

Agency Reply: Concur. See page 70.

Payroll programs be modified so that a listing is produced reflecting both changes in salary rates and master file additions or deletions. 11

Agency Reply: Concur. See page 70.

Page

Users check all file update reports against source documents. 12

Agency Reply: Do not concur. See page 71.

The payroll system be linked with the appointments system for purposes of more efficiently reviewing certification and appointment terminations. 12

Agency Reply: Concur. See page 71.

Establish procedures to ensure that all adjusting journal entries are either signed or initialed by both the preparer and authorized approver. 13

Agency Reply: Concur. See page 71.

Establish a minimum amount for processing interdepartmental cost transfers. 13

Agency Reply: Do not concur. See page 72.

A legal opinion be requested regarding the appropriateness of not allocating a portion of the $427,534 balance in the Foundation Income Account to the University. 15

Agency Reply: Do not concur. See page 72.

Assign a top priority to gaining a thorough understanding of the SBAS cash accounting and reporting system and prepare proper cash reconciliations, by fund, between general ledger and SBAS cash balances on a monthly basis. 16

Agency Reply: Concur. See page 73.

Institute procedures to ensure that cash reconciliations for local revolving bank accounts are prepared on a timely basis. 17

Agency Reply: Concur. See page 74.

The University carefully review disbursements made from the local bank accounts in order to determine if SBAS can and should be utilized for a portion of these expenditures. 17

Agency Reply: Concur. See page 74.

Page

A listing of checks received be made by the employee opening the mail. 17

Agency Reply: Concur. See page 75.

Establish more detailed written guidelines for approval of disbursements. 18

Agency Reply: Concur. See page 75.

Paid-out forms should be numerically controlled. 18

Agency Reply: Concur. See page 75.

Move toward an automated accounts receivable and billing applications which are integrated with other University accounting systems. 19

Agency Reply: Concur. See page 75.

The internal auditor make periodic confirmations of accounts receivable balances, and also that the University establish a minimum amount for which monthly statements are produced and mailed. 19

Agency Reply: Concur. See page 75.

Evaluate the feasibility of maintaining additional perpetual records for inventories and include supplies inventories at the Physical Plant and Health Services departments in year end inventory balances. 20

Agency Reply: Concur. See page 76.

Business office or internal audit personnel supervise all inventory counts. 20

Agency Reply: Concur. See page 76.

Price and cut-off tests be performed in order to help ensure accurate inventory balances. 20

Agency Reply: Do not concur. See page 76.

Invoices be maintained supporting prices for all items included in inventory and more detailed procedures be developed for pricing slow-moving stock. 20

Agency Reply: Do not concur. See page 76.

Page

Conduct a physical inventory of property, plant and equipment as soon as practicable. 21

Agency Reply: Concur. See page 77.

Adjust the University accounting records to reflect the results of the physical inventory. 21

Agency Reply: Concur. See page 77.

Establish procedures to ensure that expenditures are properly classified by developing a specific capitalization policy. 22

Agency Reply: Concur. See page 77.

Develop procedures to ensure that all property, plant and equipment additions, including donated items, are reported to the accounting department. 22

Agency Reply: Concur. See page 77.

Develop the procedures required for purposes of providing an equitable distribution of investment income and the realized gain resulting from the liquidation of pooled investments among participating funds. 23

Agency Reply: Concur. See page 78.

Simplify the method of NDSL principal and interest cancellation. 24

Agency Reply: Concur. See page 78.

Conduct, to the extent possible, exit interviews on all student borrowers and document the information received in the student's loan file. 24

Agency Reply: Concur. See page 78.

Procedures be developed to bill the federal government promptly for current and anticipated CWSP expenditures and related administrative costs. 25

Agency Reply: Concur. See page 79.

Monthly payrolls should be reviewed and approved by the payroll supervisor prior to payment. 26

Agency Reply: Concur. See page 79.

Page

A hiring and rate authorization form for part-time, non-student employees, approved by the Personnel Director, should be developed and implemented. 26

Agency Reply: Concur. See page 79.

Written guidelines for proper time card preparation, overtime authorization, and control of signature stamps should be developed and distributed to each department. 27

Agency Reply: Concur. See page 80.

New appointment forms or a status change form should be prepared and maintained in the personnel files for each change in a full-time employee's pay rate or job status. 27

Agency Reply: Concur. See page 80.

Leave accounting procedures for all University employees should be accounted for within the payroll system. 27

Agency Reply: Concur. See page 81.

Leave accounting procedures for faculty should be reviewed to determine if there are ways to improve the present "exception only" system of reporting. 27

Agency Reply: Concur. See page 81.

A special listing of monthly additions to and deletions from the payroll master file should be prepared and reviewed by payroll and personnel department supervisors. 27

Agency Reply: Concur. See page 81.

Adequate property records and procedures be developed and implemented. 28

Agency Reply: Concur. See page 81.

Consider appropriate computer programming changes to make it easier to comply with time and effort accounting and reporting requirements. 28

Agency Reply: Concur. See page 81.

Ensure that fringe benefits billed on CETA employees are correct. 29

Agency Reply: Concur. See page 82.

SUMMARY OF RECOMMENDATIONS (Continued)

	Page
Review billings for CETA employees prior to submission to the sponsoring agency.	29
Agency Reply: Concur. See page 82.	
Develop improved controls over athletic reserve seat sales at discounted prices.	30
Agency Reply: Concur. See page 82.	
Restrict access to the athletic ticket office to ticket office employees and their supervisors.	30
Agency Reply: Concur. See page 82.	
Develop written procedures for preparation and review of athletic ticket sales reconciliations.	30
Agency Reply: Concur. See page 82.	
Develop additional written procedures for preparation of print shop cost summaries and related customer billing.	30
Agency Reply: Concur. See page 83.	

Ernst & Ernst

2700 Seattle-First National Bank Bldg • 1001 Fourth Ave • Seattle, WA 98154 • Phone 206/622-0610

The Legislative Audit Committee
of the Montana State Legislature
Helena, Montana

We have completed our examination of the financial statements of the University of Montana for the year ended June 30, 1976. Our separate accountants' report on those statements appears on page 39.

Our examination included a review of system of internal control, accounting procedures and data processing activity of the University. The comments which follow are based upon conditions noted during our audit and are not intended to be all inclusive. They are submitted as constructive suggestions to assist University management in strengthening controls and procedures and have, in some instances, already been implemented. Furthermore, they are not intended to reflect upon the honesty or integrity of any employee.

We appreciate the opportunity to present these comments and recommendations for the University's consideration. Additionally, we wish to express our appreciation for the cooperation and courtesies extended to our representatives by the personnel of the University of Montana throughout our examination.

Ernst & Ernst

Seattle, Washington

May 23, 1977

E&E

Management Information System

Many of the difficulties we encountered during the course of our examination were attributable to the lack of an integrated management information system. Such important areas as payroll and accounts receivable, although partially automated, were not integrated with the University's general ledger accounting system.

Additionally, the University's primary working level management tool, the departmental ledger, was not integrated with the general ledger system. As a result of these conditions, considerable time and effort was required on the part of University personnel correcting and adjusting financial data in order to generate meaningful management reports.

We recommend the University thoroughly review and analyze its present management information system, identifying desired system improvements and enhancements, and expend such efforts as necessary in order to integrate the present costly and segmented accounting system into a comprehensive management information system. Such analysis should take into account the capabilities of the Statewide Budgeting and Accounting System.

Accounting and Budgeting Procedure Manuals

Because of the many subsystems and complexities inherent in the management information system, we observed a general lack of understanding on the part of accounting personnel regarding the

accounting system taken as a whole. Under the organizational structure existing at the time of our examination responsibility was delineated primarily on a functional basis. In this regard, we noted that some accounting supervisors were unaware of the impact that certain of their decisions had on other functional areas and how the University's system related to the Statewide Budgeting and Accounting System.

We recommend the University develop comprehensive accounting and budgeting procedure manuals. Such manuals should encompass specific procedures and techniques and, also, identify responsibility by position.

Financial Statements

Because of the numerous complexities previously discussed with respect to the University's accounting and reporting systems, complete financial statements were not prepared by the University system on a monthly basis. In fact, complete financial statements were prepared only on an annual basis. Certain revenue and expenditure details were presented in the monthly departmental ledger, but it was not always prepared on a timely basis.

We recommend the University prepare monthly financial statements on a timely basis showing (as appropriate) the financial position, revenues, expenditures and other changes, and changes in fund balances for each fund. The amount of information presented should be appropriate considering the needs of the users.

Such statements should serve as a valuable tool for purposes of managing and controlling financial activities and, additionally, be a significant resource for purposes of budget preparation.

Chart of Accounts

The general ledger chart of accounts had not been revised to reflect several significant changes, including the separation of assets from the University of Montana Foundation and the transfer of cash balances to the State Treasurer. Furthermore, many of the existing account titles were either inappropriate or misleading.

We recommend that the chart of accounts be revised in order to be more compatible with the University's organizational structure and the financial reports to be generated.

Data Processing

Our examination included an evaluation of the extent and quality of data processing internal controls for both the data processing installation and user departments. Additionally, it included an organization review of the data processing department and an application review of the payroll system. The findings which follow are either conditions or control weaknesses which we believe should be followed-up by University management, or findings which relate more to operating effectiveness or efficiency and which may represent potential rather than actual control weakness.

I. Organization

The University had not recently conducted an overall organizational review to determine if the number of employees in operations and programming was consistent with the size and complexity of hardware and the number of operations. Also, the duties actually performed in some positions (such as control clerk) did not fit the traditional definition and description of the position. We recommend that the University conduct such an organizational review of data processing activities to determine appropriate staffing levels. In connection with this review, position titles and descriptions should be clarified.

II. Security

Physical security over processing equipment needs to be improved. There are no locked doors, and the primary security measure is a computer operator being on duty for all three shifts. Such conditions could allow unauthorized access to the computer. Additionally, there is no written disaster plan (i.e., back up procedures in the event of equipment failure or natural disaster). We recommend that the University establish procedures restricting access to computer operations only to

authorized employees, and perform a detailed review of data security for purposes of identifying needed refinements. Furthermore, we recommend that a written disaster plan be developed.

III. Management

No formal continuing education program had been developed for data processing personnel. Because of rapid advancements with respect to data processing technology, we recommend the University establish a continuing education program to ensure that the level of data processing knowledge is continually kept current in both the operations and programming sections. The program should encourage employees within these sections to attend professional development courses on a regular basis.

The general consensus, on the part of both data processing personnel and users, and with which we concur, was that the systems were not adequate and were developed in a fragmented manner. Additionally, the systems and programming section felt there were many applications to revise or completely rewrite.
We recommend that the University develop a long-range

systems plan to ensure that new systems under development will easily integrate with other systems. The specifics relating to each application and how such application relates to the entire information system should be clearly set forth.

IV. Operations

The operations section manager did not sign or initial the console log to indicate review for operational problems, unusual program runs, etc. We recommend that the operations section manager sign or initial the console log to indicate that such review was made.

Other than for payroll applications, processing schedules were not adequately documented. We recommend that adequately documented input, processing and output schedules be developed for each application.

Data processing costs were not charged to user departments based on actual usage. We recommend that consideration be given to the development of a cost allocation algorithm whereby user departments can be charged based on actual usage.

V. Documentation

A standard procedure manual had not been developed and, as such, there was little cohesiveness to the documentation efforts displayed by each employee. We recommend that a manual be created establishing standards for programming, system design, management, documentation and methods.

In many instances, system documentation was incomplete. We recommend the University develop adequate procedures to ensure proper system documentation, including general narratives, system flowcharts and standard formats.

Data entry instructions were not complete documents providing all the necessary information for the operator (e.g., left zero fill indicators are missing). We recommend the University develop detailed data entry instructions.

VI. Systems and Programming

Under the processing system in effect during our examination, an automated "jobs in progress" system was not maintained, although a manual system was used. With projected increases in automated processing applications, an automated "jobs in

progress" system may become more desirable to assist in controlling time schedules and pinpointing causes of processing time overruns.

We recommend that the need for an automated "jobs in progress" system be monitored in light of current and projected levels of data processing activity.

VII. Internal Audit

The University had not developed audit programs for purposes of reviewing data processing controls and procedures. We recommend that the internal audit department develop and implement such programs.

Data Processing - Payroll Application

I. Input Controls

Source documents were not used to support all input changes. We recommend that source documents be used to support all input changes for purposes of creating an adequate audit trail.

Adding machine tapes were sometimes used for balancing purposes without a user job request form prepared and

attached. We recommend that user job request forms be prepared (with adding machine tapes attached) to assist in the balancing process.

The review made by the payroll department to ensure that input was properly processed was inadequate. We recommend that the payroll department check the information processed by data processing to verify such information as the number of timecards, number of regular and overtime hours, salary rates, etc.

II. Processing Controls

When errors occur it is often difficult to determine which batch is in error. We recommend the payroll system be modified to accept batch numbers to aid in balancing input data.

There was no automated internal program check of batch control totals, although a manual check was made. We recommend that edit routines in the payroll program include batch total checks.

For some employee classifications, certain information fields were keypunched each pay period. We recommend that certain key information fields, such as pay rates, be put

on the payroll master file at the time of employee hire, and that control procedures be established for any future changes to the file.

III. File Controls

Two separate departments, payroll and personnel, could load information into the system and neither of these departments had a clear understanding of precisely which fields were theirs to control. We recommend that specific information relating to input field controls be conveyed to each department.

Faculty salary rates were maintained on a card master file which did not provide strong control over rate changes. It would have been possible to change the rate on a card without having to "log on" the computer. Additionally, users did not maintain any overall file controls on the number of employees. It would have been relatively easy to add an unauthorized or ficticious person to a department and generate a paycheck. We recommend that payroll programs be modified so that a listing is produced reflecting both changes in salary rates and master file additions or deletions.

IV. Output Controls

Users did not always check the file update report against source documents. They generally assumed that all information sent to data processing was entered and processed correctly unless it appeared on an error report. We recommend that users check all file update reports against source documents.

At the time of our examination, the finanical aid office had to manually check the certification card for each student, each payroll. Additionally, payroll maintained a manual appointment termination system in order to prevent the sending of checks after the end of the appointment period. We recommend the payroll system be linked with the appointments system for purposes of more efficiently reviewing certification and appointment terminations.

Additional comments relating to the payroll and personnel systems are presented in a subsequent section of this letter.

Journal Entries

An unusually large number of manually prepared adjusting journal entries were noted during the course of our examination, many of

which were the result of the unwieldy management information system discussed previously. Our review also disclosed that most adjusting journal entries were neither initialed by the preparer nor the employee approving the journal entry. This weakness makes it very difficult to locate the source for adjustments and could lead to erroneous or even unauthorized entries. Additionally, we noted several journal entries which lacked adequate supporting documentation.

We recommend that the University establish procedures to ensure that all adjusting journal entries are either signed or initialed by both the preparer and authorized approver. Furthermore, the authorized approver should make certain that adequate supporting documentation exists for each journal entry.

Interdepartmental Cost Transfers

The majority of journal entries were for interdepartmental cost transfers. Many of these interdepartmental cost transfers were processed on hand prepared invoices for amounts less than one dollar. The cost of preparation and processing of such small transfer amounts may exceed any benefit derived.

We recommend that the University establish a minimum amount for processing interdepartmental cost transfers. This might involve accumulating costs transfers on a weekly or monthly basis so as to reduce the number of billings and related journal entries.

Foundation Transfers

In accordance with prior audit recommendations, the University and Foundation effected a separation from an accountability standpoint during fiscal year 1975-1976. This separation was considered to be retroactive to July 1, 1975, and amounts so divided were reflected as adjustments to beginning fund balances on the University accounting records.

The separation was complete except for certain accounts referred to as "academic development" accounts maintained on the books of the Foundation. These amounts were designated by donors to be expended by various educational departments and will be transferred to the University as requested by the departments, however, in any event the transfer will be completed by July, 1977.

In conducting the review, University and Foundation employees were able to ascertain ownership of most assets in question. However, adequate records do not exist for purposes of determining ownership of a significant account, the Foundation Income Account, presently accounted for on the Foundation's accounting records. This asset account had a cash balance of $427,534 at July 1, 1975 and represented an accumulation of investment and other income from University and Foundation assets over a period of several years. University and Foundation executives decided that this asset should remain with the Foundation.

We recommend that, because of the lack of adequate accounting records and the significance of the amount in question, a legal opinion be requested regarding the appropriateness of not allocating a portion of the $427,534 balance in the Foundation Income Account to the University.

Cash Reconciliations - SBAS

In October, 1975 the University transferred the cash balances of each fund to the State Treasurer and maintained two revolving accounts in a local bank for certain types of expenditures such as special payroll checks and vendor invoices providing discounts. A proper cash reconciliation was not prepared at the point of transfer and, additionally, no reconciliation between cash balances as shown in the general ledger and those reported by the State Treasurer was made during the entire fiscal year. This represents a serious problem from both an internal control and accounting procedure standpoint.

At our request, University accounting personnel attempted to reconcile the general ledger cash balances with those reported by the State Treasurer but they were unable to prepare a satisfactory reconciliation. A summary reconciliation, including the cash balances of all funds, resulted in an unreconciled difference of approximately $9,000 at June 30, 1976. The net amount of cash for all funds being less than that reported by the State Treasurer.

Since monthly reconciliations were not prepared throughout the year, it was not possible to determine the cause of this unreconciled difference. The unreconciled difference may have been the result of a lack of understanding regarding the SBAS system on the part of University accounting personnel and difficulties encountered by them in establishing an interface between the University general ledger accounts and SBAS accounting entities. Furthermore, the University has not yet attempted to reconcile general ledger and SBAS cash balances for any period subsequent to June 30, 1976.

We recommend the University assign a top priority to gaining a thorough understanding of the SBAS cash accounting and reporting system and prepare proper cash reconciliations, by fund, between general ledger and SBAS cash balances on a monthly basis. These reconciliations should be prepared as soon as the month end reports are generated by the SBAS system.

Cash Reconciliations - Revolving Bank Accounts

Bank reconciliations for the two revolving accounts maintained by the University were not prepared on a timely basis. We observed the average time period from receipt of bank statement to preparation of reconciliation to be approximately forty-five days. Also, a significant amount of expenditures were made from the local bank accounts.

We recommend the University institute procedures to ensure that cash reconciliations for local revolving bank accounts are prepared on a timely basis. Furthermore, we recommend the University carefully review disbursements made from the local bank accounts in order to determine if SBAS can and should be utilized for a portion of these expenditures.

Cash Receipts - Mail

Numerous checks were received by mail in the Controller's office representing payments of fees or loans. Such receipts were received by various personnel who hand delivered the checks to the cashier where they were receipted into the University's accounting system. An independent listing of cash receipts by mail was not made.

We recommend that a listing of checks received be made by the employee opening the mail. Such a listing would help strengthen internal control over cash receipts and also may be of value in situations warranting a reconstruction of cash receipts records.

Cash Disbursements

University procedures relating to non-payroll disbursements require the vendor's invoice be matched to a purchase order having a properly completed receiving report at the bottom of the form. In our testing, we noted limited instances in which the invoice amount did not agree with the amount authorized for purchase but the invoice amount was paid.

Our review of non-payroll disbursements indicated that many departments use rubber stamp signatures for purposes of authorizing disbursements. These stamps did not appear to be adequately controlled, as is necessary if unauthorized purchases are to be avoided.

When University cashiers dispense cash to recipients of student aid, the authorizing form is a "paid-out". These forms, which are processed through the cashier, were not numerically controlled, allowing the possibility of unauthorized use.

We recommend the University establish more detailed written guidelines for approval of disbursements. These guidelines should require adequate evidence to be maintained supporting each disbursement and also set forth controls relating to the use of rubber stamp signature authorizations by departments. Additionally, paid-out forms should be numerically controlled.

Accounts Receivable

As discussed previously, "memo" accounts receivable subsystems are not integrated with other University accounting and reporting systems. Receivable amounts are derived from a variety of sources and recorded in the general ledger only at year end. Additionally, certain activities such as printing and clerical generate revenue from sales of material or services to outsiders. Receivables resulting from such activities are not reflected on accounts receivable subsystems and adjustments are only made at year end to reflect these amounts.

In addition, our review disclosed that no miminum billing amount exists. Insignificant amounts (less than one dollar) are sometimes input and billed on a monthly basis.

We recommend the University move toward an automated accounts receivable and billing applications which are integrated with other University accounting systems. Furthermore, we recommend the internal auditor make periodic confirmations of accounts receivable balances, and also that the University establish a minimum amount for which monthly statements are produced and mailed.

Inventories

Only the chemistry stores department maintained a computerized perpetual inventory system. The other ending departmental inventories were determined solely by year end count. Also, it has been the policy of the University to record supplies inventories for only certain auxiliary enterprises and educational service departments. Significant amounts of supplies inventories at the Physical Plant, and Health Services departments were not counted and included in ending inventory. Purchases of the latter supply items were charged directly to current year expenditures. The University has estimated inventory amounts for these items to approximate $139,000 at June 30, 1976. The actual amount of these inventories was not determinable because no physical count was taken and the University did not maintain perpetual inventory records for these items.

Guidelines were prepared by the University Controller's office for the taking and costing of physical inventories. However, little evidence of testing existed with respect to either pricing or cut-off, and not all counts were observed by the Controller's office or internal audit personnel. Additionally, we encountered difficulty in locating invoices to support inventory prices, primarily on slow-moving stock that had been purchased in prior years.

We recommend the University evaluate the feasibility of maintaining additional perpetual records for inventories and include supplies inventories at the Physical Plant and Health Services departments in year end inventory balances. Further, we recommend that:

- Business office or internal audit personnel supervise all inventory counts.

- Price and cut-off tests be performed in order to help ensure accurate inventory balances.

- Invoices be maintained supporting prices for all items included in inventory and more detailed procedures be developed for pricing slow-moving stock.

Property, Plant and Equipment

The University does not maintain detailed records of property, plant and equipment which agree to general ledger balances, and we understand that a complete inventory of University assets has never been made. Also, we noted several inconsistencies in the accounting for capital expenditures made during the fiscal year ended June 30, 1976. Small expenditures (less than $100) and certain repairs and maintenance costs were sometimes capitalized and sometimes expended. Furthermore, it appears that equipment disposals are rarely deleted from the accounting records. As a result of these matters there is no assurance that amounts reported on the University accounting records and financial statements as property, plant and equipment are reliable.

Since the primary considerations relating to property, plant and equipment are to secure close control over capital expenditures and to obtain maximum utilization of existing equipment, we recommend the following:

- Conduct a physical inventory of property, plant and equipment as soon as practicable. All equipment inventoried should be tagged or otherwise provided an identification number.

- Adjust the University accounting records to reflect the results of the physical inventory.

- Establish procedures to ensure that expenditures are properly classified by developing a specific capitalization policy.

- Develop procedures to ensure that all property, plant and equipment additions, including donated items, are reported to the accounting department. Additionally, procedures should be established to properly account for equipment disposals.

Investment Income

Except for investments held by trustees' for Retirement of Indebtedness and Endowment and Similar Funds, most University investments during fiscal year 1975-1976 were in the short-term investment pool (STIP) managed by the Montana Board of Investments.

These investments were liquidated prior to June 30, 1976. The liquidations resulted in a gain of $170,816 which was allocated as follows:

Current funds:	
Education and general	$131,484
Auxiliary enterprises	8,500
	139,984
University of Montana Foundation	30,832
	$170,816

No amounts were allocated to other participating University funds, i.e., Current Restricted, Loan, or Plant Funds. Generally accepted accounting principles for universities require that accounting for such pooled investments should provide for an equitable distribution of investment income and the realized gain resulting from liquidation of pooled investments among the various participating funds.

We recommend the University develop the procedures required for purposes of providing an equitable distribution of investment income and the realized gain resulting from the liquidation of pooled investments among participating funds. This will require the University to maintain current cash reconciliations by fund.

National Direct Student Loans

National Direct Student Loans (NDSL) represent a major portion of the federally funded student aid administered by the University. These loans allow for a portion of the interest and principal to be cancelled based on time spent in a service function (i.e., teaching, armed forces). The University accounting system did not have the capability to easily account for loan cancellations.

Also, exit interviews are an integral part of the NDSL program. They are designed as an information exchange medium by which the University gains future address and employment information and notifies the borrower of the repayment schedule. These exit interviews are not always held, usually because of early

departure by the student and the student not returning for the next scheduled quarter. Inability to conduct these interviews could be a contributing factor to past due outstanding loans.

We recommend procedures be established to:

- Simplify the method of NDSL principal and interest cancellation.

- Conduct, to the extent possible, exit interviews on all student borrowers and document the information received in the student's loan file. This would include establishing additional written procedures in order to encourage interview attendance by the student, and procedures for follow-up on students with whom an exit interview was not possible.

College Work Study Program

During our review, we noted the College Work Study Program (CWSP) costs were being billed approximately three months after the expenses were incurred. Federal billing procedures provide the opportunity to bill for current plus one month's estimated expenses. One apparent reason for the billing delay has been the time lag in receiving departmental ledgers, however, payroll data contains the required information and is produced on a more timely basis.

We recommend that procedures be developed to bill the federal government promptly for current and anticipated CWSP expenditures and related administrative costs.

Payroll and Personnel

We noted that controls relating to the hiring and rate authorization for part-time, non-student employees were weak. All that was required to enter such individuals into the payroll system was a completed data card from the employee, together with a time card signed by the supervisor. This control problem was compounded by the fact that pay rates for all hourly employees were not loaded in the computer at the time of hiring. Rather, rates were input monthly based on amounts indicated on the time cards. During our testing, we noted instances where rates on time cards were changed with no indication of supervisory approval.

Our review of time cards disclosed several other miscellaneous problems including: student time cards not containing signatures certifying academic status; time cards being approved by use of a signature stamp; no evidence of review of authorized signatures for approval of time cards; and, no indication of authorization for overtime other than an additional time card submitted in a subsequent month.

Our review of leave records indicated that leave accounting for all employees was not done on the payroll system. Also, leave accounting for academic employees was done on an exception basis by submission of a time card only when leave was taken. Submission of time cards on an exception basis may not be sufficient to ensure that all sick leave time taken is actually reported. The portion of sick leave time accrued and payable upon termination might not be correctly calculated under the present system.

Our review of hiring authorization for full-time employees disclosed several individuals whose appointment forms (in their personnel file) were not current as to salary and/or job status.

Our review indicated that monthly additions to or deletions from the payroll master file were not listed in a separate report and reviewed by the payroll and personnel department supervisors.

We recommend the University consider the following:

- Monthly payrolls should be reviewed and approved by the payroll supervisor prior to payment.

- A hiring and rate authorization form for part-time, non-student employees, approved by the Personnel Director, should be developed and implemented. The Personnel Director should review the completed forms to ensure

that pay rates are consistent with the University standard for the particular type of work described. Additionally, rates should be loaded in the computer.

- Written guidelines for proper time card preparation, overtime authorization, and control of signature stamps should be developed and distributed to each department. The payroll department should ensure that all time cards submitted are in compliance with these guidelines, and properly authorized according to their signature file.

- New appointment forms or a status change form should be prepared and maintained in the personnel files for each change in a full-time employee's pay rate or job status.

- Leave accounting procedures for all University employees should be accounted for within the payroll system.

- Leave accounting procedures for faculty should be reviewed to determine if there are ways to improve the present "exception only" system of reporting.

- A special listing of monthly additions to and deletions from the payroll master file should be prepared and reviewed by payroll and personnel department supervisors.

The problems identified above and our recommendations are based on our review of the payroll system as it existed at the time of our examination. We understand that the University is currently in the process of changing to an integrated payroll and personnel system which may incorporate some of our recommendations.

Grants and Contracts

The University by not maintaining adequate property records, cannot properly support equipment usage charges as an element of indirect costs allowable under certain grants and contracts.

We recommend that adequate property records and procedures be developed and implemented. Such procedures are outlined in the property, plant and equipment section of this letter.

Grants or contracts usually require the preparation of time and effort reports to support personnel service costs based on the University's payroll system. We recommend that in connection with plans to revise the payroll system, the University consider appropriate computer programming changes to make it easier to comply with time and effort accounting and reporting requirements.

During our review of CETA grants administered by the University, we discovered errors in the amounts billed for fringe benefits on certain CETA employees.

We recommend that procedures be developed to:

- Ensure that fringe benefits billed on CETA employees are correct.

- Review billings for CETA employees prior to submission to the sponsoring agency.

Department Income and Recharges

Our audit included a review of procedures in effect at the intercollegiate athletics ticket office and the print shop.

Our tests of athletics ticket sales indicated:

- Adequate reconciliations of reserve seat tickets issued to sellers and related revenue received are difficult to maintain. The University offers the same type of seats at varying prices depending on the status of the purchaser (i.e., senior citizen, and student discounts or full price). The seller marks the stub as to the amount collected, but there is no internal check of this amount against the ticket stub.

- Some seller prepared ticket/revenue reconciliations had not been signed by the reviewer to indicate approval.

- We observed that access to the ticket office was not adequately restricted, in that people pass through the office to use the photocopy machine or for other purposes. This could lead to misappropriation of unused tickets.

Our tests of print shop procedures indicated that job ticket cost summaries did not always indicate details of non-paper material usage. Also, the job ticket summaries were not always prepared in a clear and consistent manner, including a description of any reductions entered before billing to the customer.

We recommend that the University:

- Develop improved controls over athletic reserve seat sales at discounted prices.

- Restrict access to the athletic ticket office to ticket office employees and their supervisors.

- Develop written procedures for preparation and review of athletic ticket sales reconciliations.

- Develop additional written procedures for preparation of print shop cost summaries and related customer billing.

Status of Legislative Auditor Recommendations for the Year Ended June 30, 1973

The majority of the Legislative Auditor recommendations for the year ended June 30, 1973 have been substantially implemented. We noted the following recommendations (from the summary of recommendations) which have not been fully implemented as of June 30, 1976:

> "Develop procedures to ensure prompt billings for federally sponsored programs."

We noted that some programs were billed on a more prompt basis, such as the AFIT program. However, written control procedures to ensure prompt billing on all sponsored programs had not been developed. We noted one grant (approximately $69,000) on which a request for cost reimbursement was not made until approximately one year after the costs were incurred.

> "Terminate the practice of paying Foundation employee payrolls with State warrants." Related to this was to terminate these employees from PERS.

This recommendation was substantially implemented effective July 1, 1976. However, one shared employee remained on the University payroll. The Foundation reimburses the University for approximately 75% of salary and related costs for this employee under a letter of understanding between the University and the Foundation.

"Comply with the provisions of Section 75-8503, R.C.M. 1947, by spending building fees for the construction of revenue producing facilities only, and seeking legislative approval for all other expenditures of student building fees."

The University has responded (progress report to the Legislative Auditor dated February 26, 1976) to this recommendation as follows: "This involves an interpretation of the Constitution and extent and nature of Regents' authority. Currently, expenditures are made in accordance with Regent policy."

"Act immediately to correct problems in its payroll system . . ."

Some specific problems referred to as a basis for this recommendation and the present status are:

- Computer programs and systems analysis for payroll had not been significantly updated since installation of a new computer in 1973. The old programs were still in use during the year ended June 30, 1976. We understand that the programs are currently in process of being re-written and/or updated.

- The computer system did not have the capability to detect abuses or test time and rate information for reasonableness. This problem was illustrated by the computer programs being able to accept unusually large hourly rates or hours.

During our review we noted that rates were still entered manually (on time cards) for certain hourly, part-time employees. We also noted the same type of hours and rate problems (i.e., lack of reasonableness tests) noted in the Legislative Auditor's report.

"Establish procedures wherein:

1. The personnel office staff meet with newly hired and terminating employees.

2. Employment and pay change authorizations are initiated in the personnel department rather than in the department which hired the employee."

We understand that a new master personnel system is being planned. However, we noted the following areas for the year ended June 30, 1976 that do not seem to have met the intent of the Legislative Auditor recommendations:

- The personnel office staff does not usually interview newly-hired non-academic staff working less than 20 hours per week. However, non-academic new hires working less than 20 hours were required to come to the personnel office and fill out a "data sheet".

- The personnel office staff did not hold exit interviews with all terminating employees. The personnel department was notified of terminations by a form submitted by the employee's department.

- We noted that various department personnel could enter (change) pay rates on certain non-academic hourly employees by entering (manually) a new rate on the time card.

"All items affecting payroll be processed through the University payroll office."

This recommendation referred primarily to input of payroll deduction data for insurance, bonds, credit union, etc., directly from various departments to data processing. We understand that this direct input was still possible during the year ended June 30, 1976.

"Board of Regents formulate a uniform policy governing benefits such as termination pay for academic employees and specify such benefits in academic contracts."

This matter was presented to the President's Council for discussion and recommendation to the Regents.

Property Accounting

"Assign responsibility for physical and accounting control of fixed assets to specific positions."

"Conduct complete physical inventories at least every two years."

"Provide control accounts for land, buildings, and office equipment in the revised property accounting system."

Although we have noted recent discussions by University personnel as to methods of complying with these recommendations, there was substantially no change in these matters for the year ended June 30, 1976. We could not audit the balances of property accounts due to a general lack of detailed records supporting general ledger balances and were unable to express an opinion as to Plant Funds.

"Properly differentiate between encumbrances and accounts payable in the financial statements."

As disclosed in the financial statements, certain encumbrances were again reported as liabilities in accordance with a Montana Department of Administration policy directive.

"Adopt sound procedures to develop financial statements, including the use of trial balances and documented adjusting and closing entries."

As previously discussed, procedures should be developed to prepare financial statements on a regular basis. Additionally, all journal entries should be appropriately documented.

"Improve control over cash disbursements by correcting internal control weaknesses."

Specific detail of these weaknesses which had not been corrected as of June 30, 1976 included:

- Signature card files for department personnel authorized to approve expenditures were not complete and were not used on a routine basis by employees who reviewed claims for payment. We discovered no signficant errors in our tests of the approval and documentation process for disbursements. But such signatures should be checked, at least on larger items.

- Revolving bank accounts are not promptly reconciled.

"Develop procedures to ensure that inventory reports produce accurate information by:

1. Supervising the taking of physical inventory.

2. Providing guidelines for costing inventory in a uniform manner.

3. Ensuring proper cut-off procedures.

4. Testing the accuracy of inventory records and making necessary corrections."

We noted improvement in these items for the year ended June 30, 1976. However, the following need further improvement:

- Not all areas having year end inventory were counted, although the controller had requested that such counts be made. As previously mentioned, significant amounts were involved.

- Procedures to ensure a proper cut-off need to be expanded and explained to various departments by the controller or internal audit office.

- Controller and/or internal audit personnel should be present to observe and make spot checks on all inventory taking if possible.

- A primary emphasis of the detail behind the recommendations was to develop accurate perpetual records in chemistry stores and clerical services. Our audit tests indicated that these records are still not completely reliable. Further, such records should be considered for all departments with significant dollar amounts of inventory.

"Institute procedures to ensure an adequate review of travel claims for compliance with State laws and regulations."

The University has complied in part with this recommendation by disseminating State travel requirements to campus users, and we discovered no variances from State regulations during our tests for the year ended June 30, 1976. However, no additional personnel were assigned to reviewing for compliance as recommended by the Legislative Auditor. We understand that additional personnel were not assigned due to a lack of funding.

Ernst & Ernst

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The Legislative Audit Committee
of the Montana State Legislature
Helena, Montana

We have examined the balance sheets of the several funds of the University of Montana as of June 30, 1976, and the related statements of changes in fund balances and current fund revenues, expenditures, and other changes for the year then ended. Except as explained in the following four paragraphs, our examination was made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances. We did not examine Plant Fund (Retirement of Indebtedness) investments and related accrued interest receivable constituting approximately 4% of Plant Fund assets, and Plant Fund (Investment in Plant) bonds payable constituting approximately 28% of total Plant Funds. These accounts were examined by another firm of certified public accountants whose report thereon has been furnished to us. Their report as it related to the above described accounts was without qualification. However, notwithstanding their report for which we assume no responsibility, certain restrictions existed on the scope of our examination as explained in the following four paragraphs.

E&E

During the year 1976, a review was conducted by employees of the University of Montana and the University of Montana Foundation (a separate corporation) for purposes of determining ownership of certain assets previously reported in the financial statements of the University of Montana Foundation. In this regard, adequate accounting records did not exist for purposes of determining ownership of cash in the amount of $427,534, the balance of the Foundation Income Account. The University and Foundation agreed that this asset should remain with the University of Montana Foundation. Because of the lack of adequate accounting records, we were unable to satisfy ourselves as to the appropriateness of this decision which, if inappropriate, could have a material effect on the financial statements of Current, Loan, and Agency Funds.

In order to comply with state fiscal laws and regulations, the University in October, 1975 transferred the cash balances of all funds to the State Treasurer. Since the transfer was made, the University has been unable to reconcile such balances, separately by fund, to those reported by the State Treasurer. Therefore, the recorded cash balances of each separate fund may or may not be correct. As of June 30, 1976, there is a net unreconciled difference for all funds combined of approximately $9,000. The total amount of cash for all funds combined was $9,000 less than that reported by the State Treasurer. Because of the lack of adequate cash reconciliations, we were unable to satisfy ourselves as to the fairness of cash balances for any of the funds, separately.

We were not present to observe the physical inventories taken at June 30, 1975 and June 30, 1976, and we have not satisfied ourselves by means of other auditing procedures concerning such inventory quantities or the costs assigned to such inventories.

Because of the inadequacy of prior year records, we were unable to obtain sufficient evidence to form an opinion regarding the property, plant and equipment balances at June 30, 1975. However, we were able to satisfy ourselves that property, plant and equipment additions for the fiscal year ending June 30, 1976, were properly stated at cost.

In accordance with a Montana Department of Adminstration policy directive, the University has recorded as expenditures and as liabilities outstanding encumbrances for equipment purchases totaling $65,187 for the year ended June 30, 1976. Also, expenditures totaling $225,819 made during the fiscal year ended June 30, 1976 relating to outstanding encumbrances for equipment purchases at June 30, 1975 were recorded as reductions of beginning fund balances. The reporting of outstanding encumbrances as expenditures and liabilities is not in accordance with generally accepted accounting principles.

The University has not included in inventory significant amounts of supplies inventories at the Physical Plant and Health Services Departments. Generally accepted accounting principles require such amounts to be included in inventory. Because no physical count or perpetual records existed for such items at June 30, 1975 or 1976, we were unable to determine the effect on the Current Fund financial statements at June 30, 1976.

University investments in the Short-Term Investment Pool (STIP) were liquidated prior to June 30, 1976. Except for the Endowment and Similar Funds, each fund participated in STIP. The liquidations resulted in a gain of $170,816 which was allocated to Current Funds ($139,984) and the University of Montana Foundation ($30,832). In accordance with University policy, no amounts were allocated to other funds. Generally accepted accounting principles for universities require that accounting for such pooled investments should provide for an equitable distribution of investment income and the realized gain resulting from liquidation of pooled investments among the various participating funds.

In our opinion, the accompanying financial statements of Endowment and Similar Funds present fairly the financial position at June 30, 1976 and changes in fund balances for the year then ended of Endowment and Similar Funds, in conformity with generally accepted accounting principles.

Because of the material effects or possible material effects on the financial statements of the matters previously discussed above, we do not express an opinion on the accompanying financial statements of Current Funds, Student Loan Fund, Plant Funds and Agency Funds for the year ended June 30, 1976.

* * * * * * * * * * * * *

Our examination was also made in accordance with the CETA Financial and Compliance Audit Guide and the provisions of the "Standards for Audit of Governmental Organizations, Programs, Activities and Functions", insofar as they related to subgrants 76-56089, 76-56057, and 76-56063. The amounts paid to the University under these subgrants totaled approximately $40,000. We identified amounts totaling $1,142 as questionable expenditures, representing charges for the full complement of fringe benefits relating to part-time CETA employees. Other than the questionable expenditures we identified, nothing came to our attention that caused us to believe that there were any events of non-compliance by the University of Montana in fulfillment of the terms of the above listed subgrants.

Ernst & Ernst

Seattle, Washington

May 23, 1977

FINANCIAL STATEMENTS

BALANCE SHEETS

UNIVERSITY OF MONTANA

June 30, 1976

ASSETS

CURRENT FUNDS	
Unrestricted:	
Education and General:	
Cash on hand, in bank and on deposit with State Treasurer	$ 473,422
Accounts receivable	5,299
Due from other funds	413,946
Prepaid expenses	97,250
Total education and general	989,917
Designated:	
Cash on hand, in bank and on deposit with State Treasurer	135,200
Accounts receivable, less allowance of $1,800	120,732
Inventories--Note D	260,440
Total designated	516,372
Auxiliary Enterprises:	
Cash on hand, in bank and on deposit with State Treasurer	592,510
Accounts receivable, less allowance of $3,200	79,047
Inventories--Note D	500,978
Total auxiliary enterprises	1,172,535
Total unrestricted	2,678,824
Restricted:	
Cash on hand, in bank and on deposit with State Treasurer	137,029
Investments--Note C	1,977
Accounts receivable	793,900
Unbilled charges	89,746
Total restricted	1,022,652
Total current funds	$3,701,476

LIABILITIES AND FUND BALANCES

CURRENT FUNDS	
Unrestricted:	
Education and General:	
Accounts payable and accrued liabilities	$ 382,368
Due to State Treasurer	199,400
Due to other funds	90,000
Deferred credits	165,310
Fund balance	152,839
Total education and general	989,917
Designated:	
Accounts payable and accrued liabilities	151,162
Due to University of Montana Foundation	48,776
Fund balance	316,434
Total designated	516,372
Auxiliary Enterprises:	
Accounts payable and accrued liabilities	125,363
Deferred credits	201,648
Fund balance	845,524
Total auxiliary enterprises	1,172,535
Total unrestricted	2,678,824
Restricted:	
Accounts payable and accrued liabilities	129,050
Due to other funds	413,946
Fund balances	479,656
Total restricted	1,022,652
Total current funds	$3,701,476

See notes to financial statements

BALANCE SHEETS

UNIVERSITY OF MONTANA

June 30, 1976

ASSETS

STUDENT LOAN FUND	
Cash on hand, in bank and on deposit with State Treasurer	$ 147,447
Investments--Note C	19,127
Loans receivable, less allowance of $149,000	2,271,685
Total student loan fund	$ 2,438,259
ENDOWMENT AND SIMILAR FUNDS:	
Investments--Note C	$ 903,564
Total endowment and similar funds	$ 903,564
PLANT FUNDS:	
Unexpended:	
Cash on hand, in bank and on deposit with State Treasurer	$ 69,179
Total unexpended	69,179
Renewals and replacements:	
Cash on hand, in bank and on deposit with State Treasurer	9,701
Total renewals and replacements	9,701
Retirement of indebtedness:	
Cash on hand, in bank and on deposit with State Treasurer	985,944
Accrued interest receivable	106,148
Investments--Note C	2,567,035
Due from other funds	90,000
Total retirement of indebtedness	3,749,127
Investment in plant:	
Land and land improvements	2,653,185
Buildings	43,420,223
Equipment	9,686,040
Library and reference books	4,480,657
Construction in progress	1,137,269
Total investment in plant	61,377,374
Total plant funds	$65,205,381
AGENCY FUNDS	
Cash on hand, in bank and on deposit with State Treasurer	$ 222,982
Investments--Note C	55,702
Accounts receivable	19,114
Total agency funds	$ 297,798

LIABILITIES AND FUND BALANCES

STUDENT LOAN FUND	
Fund Balances:	
U.S. Government grants refundable	$ 2,270,354
University funds:	
Restricted	83,556
Unrestricted	84,349
Total student loan fund	$ 2,438,259
ENDOWMENT AND SIMILAR FUNDS	
Fund balance	$ 903,564
Total endowment and similar funds	$ 903,564
PLANT FUNDS	
Unexpended:	
Fund balance	$ 69,179
Total unexpended	69,179
Renewals and replacements:	
Fund balance	9,701
Total renewals and replacements	9,701
Retirement of indebtedness:	
Accrued interest payable	262,606
Deferred credits	26,303
Fund balance	3,460,218
Total retirement of indebtedness	3,749,127
Investment in plant:	
Notes and contracts payable--Note E	17,355
Bonds payable--Note E	18,328,000
Net investment in plant	43,032,019
Total investment in plant	61,377,374
Total plant funds	$65,205,381
AGENCY FUNDS	
Deposits held in custody for others	$ 297,798
Total agency funds	$ 297,798

See notes to financial statements

CURRENT FUNDS

STATEMENT OF REVENUES, EXPENDITURES AND OTHER CHANGES

UNIVERSITY OF MONTANA

Year ended June 30, 1976

	Unrestricted			
	Education and General	Designated	Auxiliary Enterprises	Restricted
Revenues:				
Student fees	$ 4,445,402	$ 355,206		
Federal appropriations	76,398			
State appropriations	13,989,178			
Federal grants and contracts	561,571			$3,742,514
State and local grants and contracts				1,472,999
Private gifts, grants and contracts		223,241		259,225
Endowment income				9,122
Sales and services of educational activities	175,298			
Sales and services of auxiliary and designated enterprises		743,964	$6,854,472	
Other	138,606			
Total Revenues	19,386,453	1,322,411	6,854,472	5,483,860
Expenditures and transfers:				
Instruction	11,019,637			2,099,031
Research	377,586			2,351,016
Public service	220,831			
Academic support	2,481,498			9,122
Student services and aid	1,210,043	797,724		
Institutional support	1,542,913			
Operation and maintenance of plant	1,901,264			
Scholarships and fellowships	475,827			1,024,691
Auxiliary and designated enterprises		285,434	5,743,384	
Total Expenditures	19,229,599	1,083,158	5,743,384	5,483,860
Mandatory transfers for:				
Principal and interest			744,650	
Total Expenditures and Mandatory transfers	19,229,599	1,083,158	6,488,034	5,483,860

CURRENT FUNDS (Continued)

STATEMENT OF REVENUES, EXPENDITURES AND OTHER CHANGES

UNIVERSITY OF MONTANA

Year ended June 30, 1976

	Unrestricted			
	Education and General	Designated	Auxiliary Enterprises	Restricted
Other transfers and additions/ (deductions):				
Voluntary transfers for:				
Scholarships, renewals and replacements		$ (22,244)	$ (144,633)	$ 154,005
Unrestricted gifts allocated to endowment fund		(223,241)		
Excess of restricted receipts over transfers to revenues				168,580
Net Increase/(Decrease) In Fund Balances	$ 156,854	$ (6,232)	$ 221,805	$ 322,585

See notes to financial statements

STATEMENT OF CHANGES IN FUND BALANCES

UNIVERSITY OF MONTANA

Year Ended June 30, 1976

	Current Funds			
	Unrestricted			
	Education and General	Designated	Auxiliary Enterprises	Restricted
Revenues and other additions:				
Unrestricted current fund revenues	$19,386,453	$1,322,411	$6,854,472	
Student fees assessed for retirement of indebtedness				
State appropriations--restricted				
Federal grants and contracts--restricted				$4,131,128
Private gifts, grants and contracts--restricted				142,682
State and local grants and contracts--restricted				1,721,311
Investment income--restricted				16,168
Interest and recoveries on loans				
U. S. Government advances				
Expended for plant facilities (including $999,137 charged to current fund expenditures)				
Retirement of indebtedness				
Total revenues and other additions	19,386,453	1,322,411	6,854,472	6,011,289
Expenditures and other deductions:				
Educational and general expenditures	19,229,599	1,083,158		5,483,860
Auxiliary enterprise expenditures			5,743,384	
Indirect cost recoveries				358,849
Refunded to grantors				
Loan cancellations and bad debt expenses				
Administrative and collection costs				
Expended for plant facilities				
Retirement of indebtedness				
Interest on indebtedness				
Total expenditures and other deductions	19,229,599	1,083,158	5,743,384	5,842,709

Loan Funds	Endowment and Similar Funds	Plant Funds: Unexpended	Plant Funds: Renewals and Replacements	Plant Funds: Retirement of Indebtedness	Plant Funds: Investment in Plant
				$ 622,679	
		$ 66,927			
1,515	$ 1,000				
33,772					
904	14,313		$ 400	217,504	
36,297					
303,499					
					$ 1,927,587
					646,936
375,987	15,313	66,927	400	840,183	2,574,523
995	19,105				
203,109					
16,920					
			3,571	125,756	
				646,936	
				797,160	
221,024	19,105	-0-	3,571	1,569,852	-0-

STATEMENT OF CHANGES IN FUND BALANCES (Continued)

UNIVERSITY OF MONTANA

Year Ended June 30, 1976

	Current Funds			
	Unrestricted			
	Education and General	Designated	Auxiliary Enterprises	Restricted
Transfers among funds--additions (deductions)				
Mandatory				
Principal and interest			$ (744,650)	
Voluntary				
Unrestricted gift allocated to quasi-endowment fund		$ (223,241)		
Unrestricted income and plant funds allocated for:				
Scholarships		(22,244)	(131,761)	$ 154,005
Renewals and replacements			(12,872)	
Total transfers	-0-	(245,485)	(889,283)	154,005
Net Increase/Decrease In Fund Balances	156,854	(6,232)	221,805	322,585
Fund balances at beginning of year, as previously reported	178,713	-	827,199	50,462
Adjustments thereto:				
Financial separation of the University of Montana Foundation, retroactive to July 1, 1975--Note B	43,970			112,656
Correction of various errors in previously issued financial statements, reclassifications, and accounting changes--Note F	(226,698)	322,666	(203,480)	(6,047)
Fund balances at beginning of year, as restated	(4,015)	322,666	623,719	157,071
Fund balance at end of year	$ 152,839	$ 316,434	$ 845,524	$ 479,656

See notes to financial statements

Loan Funds	Endowment and Similar Funds	Plant Funds: Unexpended	Plant Funds: Renewals and Replacements	Plant Funds: Retirement of Indebtedness	Plant Funds: Investment in Plant
				$ 744,650	
	$223,241				
		$ (152)	$12,872	152	
-0-	223,241	(152)	12,872	744,802	-0-
154,963	219,449	66,775	9,701	15,133	2,574,523
2,274,943	684,115	1,995,863	-	3,810,546	40,457,496
8,353					
		(1,993,459)		(365,461)	
2,283,296	684,115	2,404	-0-	3,445,085	40,457,496
2,438,259	$903,564	$ 69,179	$ 9,701	$3,460,218	$43,032,019

NOTES TO FINANCIAL STATEMENTS

UNIVERSITY OF MONTANA

June 30, 1976

NOTE A--SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements have been prepared generally in accordance with accounting principles outlined in the American Institute of Certified Public Accountants' audit guide, "Audits of Colleges and Universities," and guidelines suggested by the National Association of College and University Business Officers. The financial statements are not comparable in certain respects with those issued in prior years due to revisions made to adhere with these accounting principles and reporting guidelines.

Fund Classifications: The accounts of the University are summarized for financial reporting purposes into the following current and noncurrent funds.

The current funds consist of the Education and General Fund, Designated Fund (use restricted by administrative policy), Auxiliary Enterprises Fund, and Restricted Fund (use restricted by donor or supporting agency). Current funds are to account for transactions related to the instructional and academic programs, including restricted purpose contracts and grants, research, extension and departmental programs, and the auxiliary activities which provide services to the student body, faculty, staff, and the public.

The noncurrent funds and their functions are described as follows: (1) Student Loan Fund is used to account for transactions related to loans to students; (2) Endowment and Similar funds are used to account for gifts which allow only the income therefrom to be expended; (3) Plant funds contain the transactions relating to investment in institutional properties and indebtedness incurred in the financing thereof; (4) Agency funds are used to account for amounts held in custody for students, University-related organizations, or others.

Accrual Accounting: The accompanying financial statements have been prepared generally on the accrual basis, except for the following practices which are common in colleges and universities: (1) vacation and sick leave are recorded as paid; (2) interest income on student loans is recorded only when received; (3) investment income is generally recorded when received; (4) gifts and pledges are recorded when received; and, (5) no provision has been made for depreciation of physical properties.

NOTE A--SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Inventories: Recorded inventories are stated at cost, first-in, first-out method. See Note D for certain inventories not recorded.

Revenue Recognition: Revenues received in connection with the current summer school are deferred at June 30.

Restricted fund revenue is recognized only to the extent expended.

Investments: Investments are stated at cost or if donated, at fair market value at date of gift.

Physical Properties: Physical properties are stated at cost or if donated, at fair market value at date of gift. Amounts expended from current funds for equipment or other capital additions are included in expenditures or transfers of such funds and are capitalized in the Plant Fund.

NOTE B--SEPARATION FROM UNIVERSITY OF MONTANA FOUNDATION

In prior years certain assets, liabilities, revenues and expenditures of the University were reported in the financial statements of the University of Montana Foundation. The Foundation is a separate Corporation formed for purposes of obtaining and disbursing funds for the benefit of the University. During the year ended June 30, 1976, a review was conducted by University and Foundation employees in order to determine the ownership of certain assets. Based on this review, certain assets were transferred to the University, retroactive to July 1, 1975. Amounts so determined are reported as changes in the beginning fund balances.

The separation process is complete except for certain accounts referred to as "academic development" accounts. These accounts were designated by donors for expenditure by various University educational departments and will be transferred to the University as requested by the departments. In July 1977, any remaining balances in the accounts will be transferred to the University. The balance of these accounts at July 1, 1975 was approximately $53,000.

NOTE C--INVESTMENTS

Investments owned by the several funds at June 30, 1976 were as follows:

	Cost	Market Value
Current restricted fund	$ 1,977	$ 1,885
Student loan fund	19,127	19,127
Endowment and similar funds	903,564	957,318
Retirement of indebtedness fund	2,567,035	2,567,035
Agency funds	55,702	56,466

The above investments consist primarily of time certificates of deposit and amounts invested with agencies of the State of Montana, but also include capital stock and bonds of publicly owned corporations.

NOTE D--INVENTORIES

It has been the policy of the University to record supplies inventories for auxiliary enterprises and certain educational and service departments. Significant amounts of supplies inventories at the Physical Plant and Health Service Departments have not been inventoried and have not been recorded in the inventory accounts. Purchases of the latter supply items have been charged directly to current year expenditures. The actual amount of these inventories is not determinable because no physical count has been taken and the University does not maintain perpetual inventory records for these items.

NOTE E--NOTES AND BONDS PAYABLE

At June 30, 1976 the University had a total of $18,328,000 in outstanding revenue bonds payable. These bonds were issued for construction of various University facilities and are summarized as follows:

- "1956 Indenture" bonds issued in ten separate series from 1956 to 1966 to build various student residence halls and apartments, remodel and add to student food service facilities, and build the University Center (a student facility). The bonds bear interest from 3.0 to 5-1/8 percent per annum.

NOTE E--NOTES AND BONDS PAYABLE (Continued)

Significant indenture requirements include that "net revenues" of the above facilities must exceed 140% of the annual principal and interest requirements of the outstanding bonds and that certain amounts be deposited to a redemption account for debt service, and to a reserve account. These requirements were met in the year ended June 30, 1976. Total outstanding bonds at June 30, 1976 were $13,756,000 and are due in varying annual installments (on July 1) through 2006. The annual debt service for the year ending June 30, 1977 is approximately $779,000. The future maximum annual debt service requirement of approximately $913,000 will be in the year ending June 30, 1997.

- "Student Buildings Fee Revenue" bonds issued in two separate series in 1963 and 1971 for purposes of renovation or building of the student health service, field house, health science, law, and liberal arts buildings. The bonds bear interest at 3-3/4 to 6.7 percent per annum. Significant indenture requirements include that certain building fees be charged to students so as to provide 135% coverage of the annual debt service requirements, and that certain amounts be deposited into redemption and reserve accounts. These requirements were met in the year ended June 30, 1976. Total outstanding bonds at June 30, 1976 were $4,085,000 and are due in varying annual installments (on July 1) through 1999. The annual debt service requirement for the year ending June 30, 1977 is approximately $340,000. The future maximum annual debt service requirement of approximately $362,000 will be in the year ending June 30, 1989.

- "Swimming Pool" revenue bonds issued in 1962 for purposes of construction of a swimming pool and facilities. The bonds bear interest at 4-1/4 percent per annum. Significant indenture requirements include that the annual net revenues of the Project and one-fourth (1/4) of the Student Activity Fee in effect at the date of the indenture will at all times be sufficient to pay principal and interest on the bonds during the year and to provide reserves in the Sinking Fund. These requirements were met in the year ended June 30, 1976. Total outstanding bonds were $169,000 at June 30, 1976 and are due

NOTE E--NOTES AND BONDS PAYABLE (Continued)

in annual installments (on July 1) through 1986. The annual debt service requirement for the year ending June 30, 1977 is approximately $21,000. The future maximum annual debt service requirement of approximately $23,000 will be in the year ending June 30, 1986.

- "Field House" revenue bonds issued in 1953 and 1956 for purposes of constructing and equipping a field house for student recreation and athletics. The bonds bear interest at 3-1/2 to 3-5/8 percent per annum. Significant indenture provisions require that the annual net income from the facilities shall be one and one-half (1-1/2) times the amount required each year to pay principal and interest on bonds, and that certain amounts be deposited into redemption and reserve accounts. These requirements were met in the year ended June 30, 1976. Total outstanding bonds at June 30, 1976 were $316,000 and are due in varying annual installments (on July 1) through 1983. The annual debt service for the year ending June 30, 1977 is approximately $57,000. The future maximum annual debt service requirement of approximately $60,000 will be in the year ending June 30, 1983.

- "Land Grant Income and Student Fee" bonds. All bonds in this issue have been called but some bonds had not been presented for payment as of June 30, 1976 in the outstanding amount of $2,000. This amount is on deposit for their redemption.

Notes payable in the amount of $17,355 consist of four notes for purchases of land and property near the University. The notes bear interest at 5-1/4 to 7-1/2 percent per annum. Two of the notes ($2,414) are due in the year ending June 30, 1977. The remaining balance of $14,941 are due in installments through 1981.

NOTE F--CHANGES IN FUND BALANCES AS PREVIOUSLY REPORTED

In order to more properly reflect University activities, several adjustments and reclassifications were made to various University fund balances as previously reported at June 30, 1975. Significant changes, in addition to the University of Montana Foundation transfer described in Note B, included the following:

NOTE F--CHANGES IN FUND BALANCES AS PREVIOUSLY REPORTED (Continued)

	Current Funds			
	Unrestricted			
	Education and General	Designated	Auxiliary Enterprises	Restricted
Reclassification of various departmental activities		$203,480	$(203,480)	
Prior period encumbrances--amounts relating to outstanding encumbrances for equipment purchases at June 30, 1975 originally recorded as payables, reversed, and charged to fund balance when paid during the year ended June 30, 1976	$(225,819)			
Correction of errors in previously issued financial statements	(879)			$(6,047)
Reclassification of accounts--associated students of the University of Montana (previously reported as a component of agency funds)		119,186		
Totals	$(226,698)	$322,666	$(203,480)	$(6,047)

	Plant Funds	
	Unexpended	Retirement of Indebtedness
Elimination of "spending authority" previously reported as an asset in the unexpended plant fund	$(1,993,459)	
Change to the accrual method of recording interest income on investments and interest expense on bonds payable		$(365,461)
Totals	$(1,993,459)	$(365,461)

NOTE G--INTEREST INCOME--SHORT-TERM INVESTMENT POOL (STIP)

Except for investments held by trustees' for Retirement of Indebtedness and Endowment and Similar Funds, most University investments during fiscal year 1975-76 were in the short-term investment pool (STIP) operated by the Montana Board of Investments.

Investments in STIP were liquidated prior to June 30, 1976. The liquidations resulted in a gain of $170,816 which was allocated as follows:

Current funds:	
Education and general	$131,484
Auxiliary enterprises	8,500
	139,984
University of Montana Foundation	30,832
	$170,816

NOTE H--RETIREMENT PROGRAMS

Retirement benefits are provided for the academic staff through the Montana Teachers' Retirement System (TRS) and non-academic staff through the Montana Public Employees' Retirement System (PERS). Both plans are operated by the State of Montana and membership is compulsory for the respective classes of employees. Contributions for participants and the University are based on a percentage of the participant's salary.

Defined benefits under both plans are based on years of service and final average salary of the participant. The actuarial present value of vested benefits and the amount, if any, of unfunded past service costs for employees covered under the plans has not been determined. The University's share of the cost of these plans for the year ended June 30, 1976 was $954,117.

NOTE I--COMMITMENTS

- Accounting for major construction projects of the University is performed by the Architectural and Engineering Bureau of the Montana Department of Administration. At June 30, 1976 certain projects had a remaining spending authority (i.e.,

NOTE I--COMMITMENTS (Continued)

funds appropriated for University building projects) from the State in excess of two million dollars. Since these funds will become available to the University only when construction costs are incurred, they have not been included in the University balance sheet as assets.

AGENCY REPLIES

University of Montana
Missoula, Montana 59812
(406) 243-0211

August 26, 1977

Mr. Morris L. Brusett
Legislative Auditor
State Capitol Building
Helena, Montana 59601

Dear Morris:

Enclosed is the University's response to the audit comments of Ernst and Ernst for the 1975-76 fiscal year. The response is being forwarded to you through the Office of the Commissioner of Higher Education. The auditor's comments and recommendations derive primarily from the correctly perceived weaknesses of the University's operating systems. It might be helpful to you and to the Legislative Audit Committee to make one or two comments about this:

1. The weaknesses in the University's financial system have been apparent for some time. Nevertheless, a coordinated approach to improvement must be taken to comply with the directives and desires of the Regents and the Legislature. The University is a wholehearted participant in the study program which will make the Statewide Budget and Accounting System responsive to the needs of the units of the Montana University System, including the University of Montana, enabling us to abandon our local system. We will progress as rapidly as this program of improvement progresses. Until then the University will be running and reconciling two accounting systems - one antiquated and inadequate, the other in need of adaptation to meet the operational and management needs of the colleges and universities.

2. You are aware that the University, during the period covered by this audit continued to simulate a number of financial subsystems - payroll, budget, accounts receivable and encumbrances - originally written for an old computer. Since these systems have become unreliable and cannot be patched further, our systems and programming resources have been dedicated for the past 8-10 months

to rewrite, with minor enhancements, the programs to run on our new computer. This has severely limited the opportunity to make any operational improvements. Essentially, this work is now complete. We anticipate this "clean-up" effort will make possible significant improvements in our daily operations.

Two comments in the Ernst and Ernst opinion letter are less than satisfactory, particularly as they are used as a basis for not issuing an opinion on the financial position of the University. While our enclosed response provides more detail, we want to point out the inappropriateness of the comments on the ownership of the Foundation Income Account and on the $9,000 balance not reconciled with the records of the State Treasurer. The auditors either should have made sufficient inquiries to take a position on the correctness of the transactions involved or should have recognized the decisions made by management in each instance.

We appreciate the opportunity to respond to the auditor's comments. If we may provide additional information, please let us know. We are returning to you the draft copies of the audit and opinion.

Very truly yours,

Richard C. Bowers

Richard C. Bowers
President

RCB:T

cc: Lawrence K. Pettit

Enclosures

AUDIT RESPONSE

University of Montana

1975-76

Management Information System

Recommendation: We recommend the University thoroughly review and analyze its present management information system, identifying desired system improvements and enhancements, and expend such efforts as necessary in order to integrate the present costly and segmented accounting system into a comprehensive management information system. Such analysis should take into account the capabilities of the Statewide Budgeting and Accounting System.

Response: Concur. This is an urgently needed improvement. The shortcomings of the University's accounting system have been well documented. The University is participating with the Office of the Commissioner of Higher Education on a project to integrate University accounting into the State's budget and accounting system (SBAS).

Accounting and Budgeting Procedure Manuals

Recommendation: We recommend the University develop comprehensive accounting and budgeting procedure manuals. Such manuals should encompass specific procedures and techniques and, also, identify responsibility by position.

Response: Concur. The Controller's Office is undergoing reorganization with responsibilities assigned for interaction with SBAS. Assignments have been made to develop an accounting manual during the current year although such development must be coordinated with the phasing out of the

existing accounting system and integration into a revised SBAS.

Chart of Accounts

Recommendation: We recommend that the chart of accounts be revised in order to be more compatible with the University's organizational structure and the financial reports to be generated.

Response: Concur. Some adjustments have been made. Due to the limitations of the present University accounting system, complete compatibility cannot be achieved. A revised and coordinated chart of accounts is needed for the Montana University System as it integrates into SBAS and the University's chart of accounts will be revised at that time.

Data Processing

I. Organization

Recommendation: We recommend that the University conduct such an organizational review of data processing activities to determine appropriate staffing levels. In connection with this review, position titles and descriptions should be clarified.

Response: Partial Concurrence. A review of the systems analysis and programming section was, in fact, underway prior to the time of the audit. The review has resulted in the subsequent implementation of several changes in the staffing and organization of that section. Further organizational changes for that section are being considered for implementation in the near future. A review of operational and production functions was begun subsequent to the audit. Resultant recommended changes are just reaching the implementation stage. It should be noted that the University has no control over

position titles and descriptions for state classified positions.

II. Security

Recommendation: We recommend that the University establish procedures restricting access to computer operations only to authorized employees, and perform a detailed review of data security for purposes of identifying needed refinements. Furthermore, we recommend that a written disaster plan be developed.

Response: Concur. Improved security controls, including more restricted access, locked doors, backup procedures, etc., are being developed in conjunction with the University's upgrade to its new computer system. A written disaster plan will be developed.

III. Management

Recommendation: Because of rapid advancements with respect to data processing technology, we recommend the University establish a continuing education program to ensure that the level of data processing knowledge is continually kept current in both the operations and programming sections. The program should encourage employees within these sections to attend professional development courses on a regular basis.

Response: Partial Concurrence. A formal continuing education program has not been developed, primarily due to lack of funds to support such a program. Because of the nature of the present Computer Center organization and the present computing hardware, we see no need for a program for the operations area, nor do such programs seem to be

available which are suitable for timesharing computer hardware. However, continuing education programs for systems analysts and programmers are highly desirable, and will be developed when sufficient funding becomes available.

Recommendation: We recommend that the University develop a long-range systems plan to ensure that new systems under development will easily integrate with other systems. The specifics relating to each application and how such application relates to the entire information system should be clearly set forth.

Response: Concur. The University is aware of the need to renovate its administrative applications systems as evidenced in recent upgrades in computing hardware and the administrative systems and programming staff. For the past year, an advisory committee has been reviewing needs and priorities in the area of administrative data processing applications, and a long-range plan is being developed. This plan will be coordinated with those of other units through the Office of the Commissioner of Higher Education.

IV. Operations

Recommendation: We recommend that the operations section manager sign or initial the console log to indicate that such review was made.

Response: Partial Concurrence. While regular review of console logs is, of course, desirable, and has been practiced daily for many years, it cannot provide the type of control mechanism suggested by

the audit report. Information about program runs is not generally contained in the console log (nor should it be for a timeshared computer, where programs are seldom run under direct supervision of the computer operator). Rather, a production logbook is maintained and reviewed, as are files containing detailed program production run log sheets. These logs will be initialled in the future to indicate review by personnel concerned with the production quality control.

Recommendation: We recommend that adequately documented input, processing and output schedules be developed for each application.

Response: Concur. However, the basic observation behind this recommendation is incorrect. Other applications have been scheduled and documented for many years. Such applications where schedules are known well in advance include student registration, Regents' status reporting, grade reporting, claims and receipt processing, etc. It is perhaps true that users do not generally have access to comprehensive processing schedules, but such is the nature of timeshared computing. We will work to ensure that schedules which exist are accurate and adequately documented, and to see that schedules are as comprehensive as possible.

Recommendation: We recommend that consideration be given to the development of a cost allocation algorithm whereby user departments can be charged based on actual usage.

Response: Partial Concurrence. Data processing costs have been accounted for (although not directly charged back) on the basis of

actual usage by user department since 1972. The decision to not charge directly to using departments was a University policy decision, which we feel was entirely appropriate and correct for the period of time under consideration. Based on the mandate to achieve uniformity of accounting within the Montana University System this decision is being reviewed. Plans to implement a charge-back system are being actively considered.

V. Documentation

Recommendation: We recommend that a manual be created establishing standards for programming, system design, management, documentation and methods.

Response: Concur. A Standards and Procedures Manual, covering all areas of Computer Center activity, is presently under development.

Recommendation: We recommend the University develop adequate procedures to ensure proper system documentation, including general narratives, system flowcharts and standard formats.

Response: Concur. Coincident with the development of new administrative data processing applications and with the development of the aforementioned Standards and Procedures Manual, more thorough, uniform system documentation will be developed.

Recommendation: We recommend the University develop detailed data entry instructions.

Response: Concur. As indicated above for system documentation,

data entry instructions will be made more complete where required.

VI. Systems and Programming

Recommendation: We recommend that the need for an automated "jobs in progress" system be monitored in light of current and projected levels of data processing activity.

Response: Concur. We have occasionally discussed the development of an automated "jobs in progress" system; however, we have not felt the need for such system was great enough that a high developmental priority was warranted. We will continue to monitor the need for such a system.

VII. Internal Audit

Recommendation: We recommend that the internal audit department develop and implement such programs (for purposes of reviewing data processing controls and procedures).

Response: Concur. This audit will be incorporated into the Internal Auditor's work program in 1977-78.

Data Processing - Payroll Application

I. Input Controls

Recommendation: We recommend that source documents be used to support all input changes for purposes of creating an adequate audit trail.

Response: Concur. This recommendation was implemented with the rewrite of the simulated payroll system completed in March, 1977. Individual source documents are used for classified employees. The

employment report of the Board of Regents is used as the source document for contractual employees.

Recommendation: We recommend that user job request forms be prepared (with adding machine tapes attached) to assist in the balancing process.

Response: Concur. Job request forms have been in use for several years; however, there is no provision for a control total on the form. The form will be modified to include control data.

Recommendation: We recommend that the payroll department check the information processed by data processing to verify such information as the number of timecards, number of regular and overtime hours, salary rates, etc.

Response: Concur. Some additional controls have been implemented; however, further improvement is needed which will be incorporated when the Montana University System goes to an after-the-fact payroll as required by SB 104. This is scheduled for 1977-78 implementation.

II. Processing Controls

Recommendation: We recommend the payroll system be modified to accept batch numbers to aid in balancing input data.

Response: Concur. The ability to accept batch numbers will be provided in the payroll rewrite required to comply with SB 104.

Recommendation: We recommend that edit routines in the payroll program include batch total checks.

Response: Concur. A manual visual verification of batch totals does take place. We will attempt to make this verification automatic in 1977-78.

Recommendation: We recommend that certain key information fields, such as pay rates, be put on the payroll master file at the time of employee hire, and that control procedures be established for any future changes to the file.

Response: Concur. See also the University's response to the recommendation on page 26 of the Ernst and Ernst comments. The recommendation will require a programming change in the master personnel file so that it becomes the source of information for the rate of pay. This change will be made in 1977-78.

III. File Controls

Recommendation: We recommend that specific information relating to input field controls be conveyed to each department (payroll and personnel).

Response: Concur. This recommendation was substantially implemented with the completion of the master personnel file and the rewrite of payroll programs.

Recommendation: We recommend that payroll programs be modified so that a listing is produced reflecting both changes in salary rates and master file additions or deletions.

Response: Concur. Change information is now provided. Additions

or deletions will be included with changes required for compliance with SB 104.

IV. Output Controls

Recommendation: We recommend that users check all file update reports against source documents.

Response: Nonconcurrence. We do agree that control totals for such changes need to be checked and this is now done. In addition, all items sent to data processing for input are keypunched and verified. Consequently, we do not feel it is necessary to check all transactions against source documents.

Recommendation: We recommend the payroll system be linked with the appointments system for purposes of more efficiently reviewing certification and appointment terminations.

Response: Concur. Presently, the termination date of employees is reported by the master personnel file which payroll then uses to submit changes. To provide student certification by computer will require extensive modifications to the systems for student records, financial aids, and personnel. This will be considered in the plan for systems development.

Journal Entries

Recommendation: We recommend that the University establish procedures to ensure that all adjusting journal entries are either signed or initialed by both the preparer and authorized approver. Furthermore, the authorized approver should make certain that adequate supporting

documentation exists for each journal entry.

Response: Concur. Procedures were established and the journal voucher adjustment form revised in December, 1976. The revision provides for documentation and approval of those journal entries which are not of an interdepartment, cost transferring nature.

Interdepartmental Cost Transfers

Recommendation: We recommend that the University establish a minimum amount for processing interdepartmental cost transfers.

Response: Nonconcurrence. Implementation of this recommendation would reduce the accuracy of interim financial reports and would place additional record keeping workload on departments providing the service. We do agree that we must find a less costly method of recording these items to reduce the volume of journal entries.

Foundation Transfers

Recommendation: We recommend that, because of the lack of adequate accounting records and the significance of the amount in question, a legal opinion be requested regarding the appropriateness of not allocating a portion of the $427,534 balance in the Foundation Income Account to the University.

Response: Nonconcurrence. While we will be glad to cooperate with a legal review of this matter, we do not feel it is necessary. Adequate data are available to justify the decision made by the management of the University and the Foundation. The account which emerged as the Foundation Income Account in 1971 had a history of inconsistent

treatment of activities and changing account structures making it difficult to follow the threads of what happened. It is, however, possible to trace the experience of the Foundation Income Account since its establishment, including its beginning balance. In summary, direct and indirect expenditures on behalf of the University by the Foundation and foregone income more than compensate for the University's claim on the $427,534 balance retained by the Foundation. We will discuss this matter in detail with the Legislative Auditor to determine the proper course of action.

Cash Reconciliations - SBAS

Recommendation: We recommend the University assign a top priority to gaining a thorough understanding of the SBAS cash accounting and reporting system and prepare proper cash reconciliations, by fund, between general ledger and SBAS cash balances on a monthly basis. These reconciliations should be prepared as soon as the month-end reports are generated by the SBAS system.

Response: Concur. It must be emphasized that the true solution to this problem is adoption of SBAS as the University's accounting system eliminating the reconciliation problem. This depends on the progress of the coordinated effort currently underway to make the necessary changes in SBAS. In the meantime, cash reconciliation is a top priority item second only to those items which are required to keep the University operating. We have reconciled all 1976-77 expenditures to SBAS and have been able to determine that all cash collected during this period has been properly deposited with the

State Treasurer. In addition, cash has been reconciled for some activities for the period ended June 30, 1977. Cash reconciliations for the balance are being given top priority. Our goal for 1977-78 is a monthly reconciliation.

With respect to the $9,000 item cited by Ernst and Ernst, a significant effort was made for several months to make this reconciliation. It was management's decision that it was more important to reconcile 1976-77 than to spend further reconciliation effort in 1975-76, particularly since the balance in the Treasurer's records was in excess of the amount shown by the University. We do not feel the $9,000 is of sufficient materiality to justify the auditors' decision not to render an opinion on the University's financial operations. So far as we know, no effort was made by the auditors to determine whether the error could lie with the Treasurer's records rather than with the University so that only one-half of the equation was examined.

Cash Reconciliations - Revolving Bank Accounts

Recommendation: We recommend the University institute procedures to ensure that cash reconciliations for local revolving bank accounts are prepared on a timely basis. Furthermore, we recommend the University carefully review disbursements made from the local bank accounts in order to determine if SBAS can and should be utilized for a portion of these expenditures.

Response: Concur. Timely reconciliation is dependent upon the availability of timely reports which, hopefully, will be available

with the new accounting system.

Cash Receipts - Mail

Recommendation: We recommend that a listing of checks received be made by the employee opening the mail.

Response: Concur. Implementation will require additional resources which presently are not available to the Controller.

Cash Disbursements

Recommendation: We recommend the University establish more detailed written guidelines for approval of disbursements. These guidelines should require adequate evidence to be maintained supporting each disbursement and also set forth controls relating to the use of rubber stamp signature authorizations by departments. Additionally, paid-out forms should be numerically controlled.

Response: Concur. This problem will be addressed after the cash reconciliation goal is achieved. The reorganization of the Controller's Office will help in achieving this goal.

Accounts Receivable

Recommendation: We recommend the University move toward an automated accounts receivable and billing applications which are integrated with other University accounting systems. Furthermore, we recommend the internal auditor make periodic confirmations of accounts receivable balances, and also that the University establish a minimum amount for which monthly statements are produced and mailed.

Response: Concur. The systems changes must be coordinated with the SBAS conversion project. The internal auditor will make periodic checks of account balances.

Inventories

Recommendation: We recommend the University evaluate the feasibility of maintaining additional perpetual records for inventories and include supplies inventories at the Physical Plant and Health Services departments in year-end inventory balances.

Response: Concur. We will evaluate the need for additional perpetual inventories. Our present feeling is that they are unnecessary nor do we have the resources for such inventories.

Recommendation: We recommend that business office or internal audit personnel supervise all inventory counts.

Response: Concur. The internal auditor was present during a portion of all recorded inventories taken for the period ending June 30, 1977.

Recommendation: We recommend that price and cut-off tests be performed in order to help ensure accurate inventory balances.

Response: Nonconcurrence. Traditionally, this function has been performed by external auditors. The University currently does not have resources available to implement this program.

Recommendation: We recommend that invoices be maintained supporting prices for all items included in inventory and more detailed procedures be developed for pricing slow-moving stock.

Response: Nonconcurrence. While agreeing with the concept of having adequate data, a log of items, by vendor, would be a less expensive system.

Property, Plant and Equipment

Recommendation: Since the primary considerations relating to property, plant and equipment are to secure close control over capital expenditures and to obtain maximum utilization of existing equipment, we recommend the following:

- Conduct a physical inventory of property, plant and equipment as soon as practicable. All equipment inventories should be tagged or otherwise provided an identification number.
- Adjust the University accounting records to reflect the results of the physical inventory.
- Establish procedures to ensure that expenditures are properly classified by developing a specific capitalization policy.
- Develop procedures to ensure that all property, plant and equipment additions, including donated items, are reported to the accounting department. Additionally, procedures should be established to properly account for equipment disposals.

Response: Concur. The University has had a property inventory underway for the past several months. If resources can be made available, this effort will be carried to completion. We also anticipate

being part of the property accounting system being developed by the State, utilizing policies and procedures developed for that system.

Investment Income

Recommendation: We recommend the University develop the procedures required for purposes of providing an equitable distribution of investment income and the realized gain resulting from the liquidation of pooled investments among participating funds. This will require the University to maintain current cash reconciliations by fund.

Response: Concur. We already have this capability. Investment income in prior years had been used to support the general fund appropriation. The final year of this support was budgeted in 1976-77. Income henceforth will be distributed to the participating funds.

National Direct Student Loans

Recommendation: We recommend procedures be established to:

- Simplify the method of NDSL principal and interest cancellation.
- Conduct, to the extent possible, exit interviews on all student borrowers and document the information received in the student's loan file. This would include establishing additional written procedures in order to encourage interview attendance by the student, and procedures for follow-up on students with whom an exit interview was not possible.

Response: Concur. Changes have been made in procedures and the chart

of accounts which have produced better reporting information for Federal reports. Exit interviews are conducted with as many students as possible. Attempts are made to notify all students of their responsibility to attend an exit interview. Further follow-up procedures will be developed as resources permit.

College Work Study Program

Recommendation: We recommend that procedures be developed to bill the Federal government promptly for current and anticipated CWSP expenditures and related administrative costs.

Response: Concur. The lack of timeliness in the financial report system delays the obtaining of data for timely billings. Implementation of the new accounting system will alleviate this problem.

Payroll and Personnel

Recommendation: Monthly payrolls should be reviewed and approved by the payroll supervisor prior to payment.

Response: Concur. The payroll supervisor currently reviews the payroll prior to its release. The release indicates approval.

Recommendation: A hiring and rate authorization form for part-time, non-student employees, approved by the Personnel Director, should be developed and implemented. The Personnel Director should review the completed forms to ensure that pay rates are consistent with the University standard for the particular type of work described. Additionally, rates should be loaded in the computer.

Response: Concur. The Personnel Office will institute a procedure requiring departments to receive approval prior to hiring part-time, non-student employees. An hourly rate schedule will be prepared for such positions. Part-time employees will be processed through Personnel prior to beginning their employment and an employment form completed at that time.

Recommendation: Written guidelines for proper time card preparation, overtime authorization, and control of signature stamps should be developed and distributed to each department. The payroll department should ensure that all time cards submitted are in compliance with these guidelines, and properly authorized according to their signature file.

Response: Concur. These guidelines will be included in the Personnel Policy Manual currently being developed. Particular attention will be directed to the use of signature stamps.

Recommendation: New appointment forms or a status change form should be prepared and maintained in the personnel files for each change in a full-time employee's pay rate or job status.

Response: Concur. Presently, any change which occurs after the beginning of a new fiscal year is reflected by an adjustment to the personnel file. Changes which coincide with the start of a fiscal year have been implemented through the budget file and no record is placed in the employee's individual personnel file. This deficiency will be corrected.

Recommendation: Leave accounting procedures for all University employees should be accounted for within the payroll system.

Response: Concur. Current leave balances appear on each employee's paycheck stub.

Recommendation: Leave accounting procedures for faculty should be reviewed to determine if there are ways to improve the present "exception only" system of reporting.

Response: Concur. Procedures currently are under review with particular concern for use of sick leave by faculty members. A policy will be issued this fall.

Recommendation: A special listing of monthly additions to and deletions from the payroll master file should be prepared and reviewed by payroll and personnel department supervisors.

Response: Concur. Additional programming will be required which will be scheduled during 1977-78.

Grants and Contracts

Recommendation: We recommend that adequate property records and procedures be developed and implemented. Such procedures are outlined in the property, plant and equipment section of this letter.

Response: Concur. However, the University has been successful in getting recognition of its equipment charges from Federal negotiators.

Recommendation: We recommend that in connection with plans to revise

the payroll system, the University consider appropriate computer programming changes to make it easier to comply with time and effort accounting and reporting requirements.

Response: Concur. The University is strengthening its time and effort administration through reorganization of the Controller's Office.

Recommendation: We recommend that procedures be developed to:

- Ensure that fringe benefits billed on CETA employees are correct.
- Review billings for CETA employees prior to submission to the sponsoring agency.

Response: Concur. The error cited by the auditor has been corrected.

Department Income and Recharges

Recommendation: We recommend that the University:

- Develop improved controls over athletic reserve seat sales at discounted prices.
- Restrict access to the athletic ticket office to ticket office employees and their supervisors.
- Develop written procedures for preparation and review of athletic ticket sales reconciliations.

Response: Concur. Controls will be reviewed for possible improvement. Access to the ticket office will be restricted to employees and individuals

having official business with the office. The ticket manager will develop and publish procedures for ticket sales reconciliations. Ticket sale/revenue reconciliations will be reviewed by and initialed by the ticket manager.

Recommendation: We recommend that the University develop additional written procedures for preparation of print shop cost summaries and related customer billing.

Response: Concur. In 1976-77 the University added an accountant in the print shop. Job tickets currently are being prepared in a proper manner.

Status of Legislative Auditor Recommendations for Year Ended June 30, 1973

As indicated by the auditor, the University has substantially implemented the recommendations contained in the June 30, 1973 audit. The auditor makes several observations without making specific recommendations. Some of these observations require no comment unless there are further questions. Others are on topics more fully covered in the body of the response and are responded to in that context. Observations which need further clarification are responded to below:

Observation: We noted one grant (approximately $69,000) on which a request for cost reimbursement was not made until approximately one year after the costs were incurred.

Response: The request for reimbursement could not be made until the final report on the results of the grant work was submitted to the sponsoring agency.

Observation: It was still possible in 1975-76 for departments directly to input payroll deduction items.

Response: This is no longer possible. All items are processed through payroll.

Observation: Signature card files for department personnel authorized to approve expenditures were not complete and were not used on a routine basis by employees who reviewed claims for payment.

Response: In 1976-77 the internal auditor completed a review and updating of all signature cards. Spot checks will continue to be made to assure that the cards are kept current.

THE MONTANA UNIVERSITY SYSTEM
33 SOUTH LAST CHANCE GULCH
HELENA, MONTANA
59601

COMMISSIONER OF HIGHER EDUCATION

August 29, 1977

Mr. Morris L. Brusett
Legislative Auditor
State Capitol
Helena, MT 59601

Dear Mr. Brusett:

I have reviewed the response to the audit report of the University of Montana for the period ended June 30, 1976, prepared by Dr. Bowers. I agree, in general, with the position taken by the University.

Sincerely,

Lawrence K. Pettit
Commissioner of Higher Education

LKP:mm
cc: Richard Bowers
Ron Near

HE MONTANA UNIVERSITY SYSTEM CONSISTS OF THE UNIVERSITY OF MONTANA AT MISSOULA, MONTANA STATE UNIVERSITY AT BOZEMAN, MONTANA COLLEGE OF MINERAL SCIENCE AND TECHNOLOGY AT BUTTE, WESTERN MONTANA COLLEGE AT DILLON, EASTERN MONTANA COLLEGE AT BILLINGS AND NORTHERN MONTANA COLLEGE AT HAVRE.